No. 22,290

IN THE

United States Court of Appeals

FOR THE NINTH CIRCUIT

JOHNS-MANVILLE SALES CORPORATION,
a Delaware corporation,

Appellant,

vs.

ELLSWORTH H. EWALD, aka E. H. EWALD,
dba EWALD CONTRACTING COMPANY, and
RELIANCE INSURANCE COMPANY, a Pennsylvania
corporation, as successor in interest to
Standard Accident Insurance Company
a Michigan corporation,

Appellees.

REPLY BRIEF OF APPELLANT
JOHNS-MANVILLE SALES CORPORATION

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ERRATUM

ARGUMENT

I. Denial of Appellant's Motion for Summary Judgment was reversible error where a final judgment was entered, there existed no genuine issue of material fact and Appellant was entitled to judgment as a matter of law. 3

II. Under Arizona law, a contract incorporated into a bond must reveal only that the parties intended the con tract to benefit a third person or some class of which he is a member in order to give the third party a right to sue on the bond. 3

III. Article 11 of the specific job contract and the Award of Bid Letter which were expressly incorporated into the bond and made a part thereof converted the performance bond into a payment bond upon which Appellant can recover. 7

IV. Appellant is also entitled to recover on the performance bond because the bond was intended to benefit Appellant, and Ewald, by not furnishing a performance and payment bond and by not furnishing material as contemplated by the contract, breached two conditions of the contract, full performance of which was guaranteed by the bond. 10

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ERRATUM

Before replying to Appellee's brief, Appellant would like to direct the Court's attention to a typographical error which appears at page 18, line 5 of Appellant's Opening Brief. Use of the word "because" in that line was erroneous; the word "became" should be inserted in place of "because."

APPELLANT'S REPLY

In its Opening Brief, Appellant set forth three theories under each of which it was, as a third party beneficiary of the bond and contract incorporated therein, entitled to judgment as a matter of law. These three theories were as follows.

1. The Arizona Supreme Court's decision in *Porter v. Eyer,* 80 Ariz. 169, 294 P.2d 661 (1956) compels a ruling that the performance bond was converted, by virtue of Article 11 of the Contract and the Award of Bid Letter which were specifically incorporated into the bond and made a part thereof, into a performance and payment bond for Appellant's benefit and Appellant was therefore entitled to recover on this bond.

2. Appellant, by supplying material to a contractor for installation on public property became entitled, under the authority of *Webb v. Crane Company,* 52 Ariz. 299, 80 P.2d, 698 (1938), to recover on the performance bond because the bond contained a condition for Appellant's benefit and because the same public policy considerations which led the Court in *Webb* to allow a materialman to recover on the contractor's performance bond there are also present here.

3. Even if the bond was strictly a performance bond, Appellant, as a third party beneficiary thereof, was entitled to recover on the bond because the contractor, by failing to post a performance and payment bond and by failing properly to furnish the goods called for under the contract, did not fully perform the contract, full performance of which was guaranteed by the bond.

Appellee in its brief introduced nothing to disprove Appellant's right to recover under any of these three theories.

ARGUMENT ONE

DENIAL OF APPELLANT'S MOTION FOR SUMMARY JUDGMENT WAS REVERSIBLE ERROR WHERE A FINAL JUDGMENT WAS ENTERED, THERE EXISTED NO GENUINE ISSUE OF MATERIAL FACT AND APPELLANT WAS ENTITLED TO JUDGMENT AS A MATTER OF LAW.

Appellant agrees with Appellee that, as a general rule, an order denying a Motion for Summary Judgment is an interlocutory, nonappealable order. This general rule is not, however, applicable here where there were cross-motions for summary judgment and, pursuant to Appellee's motion, a final judgment, rather than a simple interlocutory order, was entered.

There are no genuine issues of material facts here. Neither party has contended that there are. Hence, there is nothing to be gained from an order simply reversing the trial court's judgment for Appellee and remanding the case for trial. There are no facts to be tried. Under these circumstances, if this Court is persuaded that there exist no genuine issues of material fact and that Appellant is entitled to summary judgment as a matter of law, it can and should enter an order reversing the judgment of the trial court and directing that judgment be entered for Appellant on its Second Motion for Summary Judgment. See 6 J. Moore, Federal Practice, 56.13, at 2251-52 (2d ed. 1965).

ARGUMENT TWO

UNDER ARIZONA LAW, A CONTRACT INCORPORATED INTO A BOND MUST REVEAL ONLY THAT THE PARTIES INTENDED THE CONTRACT TO BENEFIT A THIRD PERSON OR SOME CLASS OF WHICH HE IS A MEMBER IN ORDER TO GIVE THE THIRD PARTY A RIGHT TO SUE ON THE BOND.

Appellee asserts in argument II A of its brief that under Arizona law a third person can recover on a contract only if the

contract reveals that the parties intended to give the third party a direct right of action on the contract. This assertion is incorrect. To recover on a bond or contract under Arizona law, a third party must show only that the contract reveals that the parties to it intended that the third party should benefit directly from the contract. If the contract reveals such an intention, the third party is, as a matter of law, entitled to sue the surety and recover on the bond. *Porter v. Eyer,* 80 Ariz. 169, 294 P.2d 661 (1956); *Webb v. Crane Co.,* 52 Ariz. 299, 80 P.2d 698 (1938); *Ed Stearman and Sons, Inc. v. State ex rel. Union Rock and Materials Co.,* 1 Ariz. App. 192, 400 P.2d 863 (1965).

These three cases are the only Arizona cases dealing with a third party's attempt to reach a performance bond and, in each case, the criterion for recovering was whether the contract and/or bond contained conditions for the third party's benefit, his right to sue on the bond following as a matter of law if a condition for his benefit was found. Hence, Appellee's assertion that the contract must reveal an intent to give the third party a right of action on the contract is misleading and incorrect.

Appellee's third argument, on pages 12-13 of its brief, is similarly erroneous. There, Appellee asserts that:

> In the case of surety bonds, the requisite intention to benefit third-party materialmen must, in the absence of an express provision that the bond is for their benefit, be manifested by a condition for their direct payment.

However, none of the three Arizona cases dealing with a third party's rights under a performance bond requires that the intent to benefit third persons be manifested either by an express provision that the bond is for their benefit or a condition for their direct payment. On the contrary, the Supreme Court merely stated in *Porter* that:

> In order that a suit be maintainable on a contractor's bond by or for the use of a materialman the bond must be construed so as to include the materialman within its coverage,

i.e., to give him some beneficial interest therein. *Porter v. Eyer,* 80 Ariz. 169, 171, 294 P.2d 661, 662 (1956).

This statement as to how the requisite intent must be manifested is not nearly as severely limited as Appellee contends in its third argumenr. Nowhere did the Arizona Supreme Court in either *Porter* or the *Webb* case, decided earlier, limit third parties in surety cases to only two methods of proving an intent to benefit third parties. For, not only did the court in *Porter* set forth the much more general requirement that the third party show that the bond was intended "to give him some beneficial interest," but the Court found that the statutory requirement that the contractor post a performance and payment bond was a sufficient expression of intent to benefit materialmen to enable them to sue on the bond and recover from the surety. Likewise, in *Webb*, the Court did not even intimate that proof that the bond contains a condition for the putative third party's benefit must be accomplished by one of the two methods which Appellee now asserts are essential. Instead, the Court held only that in order to recover on the bond as a third party beneficiary thereof, the materialman must show, by any means available, that the bond contains a condition for his benefit.

Several additional points must be made concerning Appellee's third argument. First, after supposedly limiting its discussion to Arizona cases involving surety bonds, Appellee asserts that "contracts lacking *both* an express statement of intention to benefit third persons *and* a promise to pay them directly have been held to afford materialmen no right of action thereon." (Appellee's Brief 13.) Yet, none of the cases cired in support of this assertion is a surety case.

Second, in argument III A, Appellee states that the bonds involved in *Webb* and *Stearman* were statutory bonds which were by their express terms conditioned on payment of materialmen. Appellee then asserts that since the instant bond was not a statutory bond, legislative intent has no place in its construction.

Appellant, of course, agrees with both of these assertions. Appellant has never contended that the statutory bonds in *Webb* and *Stearman* were not conditioned on payment. Appellee, however, has not responded to Appellant's argument regarding the manner in which the *Webb* case relates to the instant case.

Briefly, Appellant utilized *Webb* to demonstrate that application of the type of reasoning and public policy considerations enunciated in *Webb* to the facts presented by the instant case would establish two points. First, the contract incorporated into the bond in the instant case was, as a matter of law, intended to benefit third parties such as Appellant. In addition, the type of public policy considerations which encouraged a holding that the subcontractor's materialmen in *Webb* should be allowed to recover on the contractor's performance bond were present in the instant case, since the work involved here was done on public property. Consequently, the *Webb* rationale affords a second, independent grounds for holding, as a matter of Arizona law, that Appellant was a third party beneficiary of the contract and bond involved herein and entitled to recover on the bond and contract. Appellee did not, however, address itself to this interpretation and use of *Webb*.

Finally, Appellee states at page 17 of its brief that the bond involved in the instant appeal is "conditioned only upon 'performance' of a contract whereby the contractor is to 'furnish' materials . . . ." and that it is, therefore, similar to the bond involved in *Porter* without benefit of the statute which the Court read into the *Porter* bond. This assertion overlooks the fact that the contract also required the contractor to furnish a performance and payment bond and that the contract was expressly incorporated into the bond and made a part thereof. With this contractual requirement read into the bond, this bond, like the bond in *Porter,* became conditioned on payment as well as performance and Appellant is entitled to recover on it as a third party beneficiary.

ARGUMENT THREE

ARTICLE 11 OF THE SPECIFIC JOB CONTRACT AND THE AWARD OF BID LETTER WHICH WERE EXPRESSLY INCORPORATED INTO THE BOND AND MADE A PART THEREOF CONVERTED THE PERFORMANCE BOND INTO A PAYMENT BOND UPON WHICH APPELLANT CAN RECOVER.

In its first three arguments, Appellee completely ignores the fact that by article 11 of the contract the telephone company was given the option of requiring that a performance and payment bond be executed and that, by the Award of Bid Letter, this option was exercised and a performance and payment bond was contractually required. Consequently, in its first three arguments Appellee consistently characterizes the contract and bond as requiring *only* that Ewald "furnish" certain materials. Not until argument IV does Appellee purport to deal with the uncontroverted fact that the contract, by virtue of the Award of Bid Letter which was incorporated therein, required Ewald, the contractor, to execute a performance and payment bond.

In its fourth argument, Appellee asserts that the performance bond could not have been converted into a performance and payment bond. Appellee offers no analytical reasons as to why the bond, by expressly incorporating the contract into the bond and making it a part thereof, could not have been converted into a performance and payment bond. Instead, Appellee supports its position by citing and quoting from several anachronistic federal decisions and one old Rhode Island opinion. Only two of the federal decisions and the Rhode Island case are actually relevant to the instant problem.

In the relevant federal cases, *Babcox & Wilson v. American Surety Company,* 236 Fed. 340 (8th Cir. 1916), and *United States ex. rel. Stallings v. Starr,* 20 F.2d 801 (4th Cir. 1927), materialmen were suing on contractor's performance bonds. The bonds did not contain any payment conditions but both bonds

were executed at a time when a federal statute required that on all government jobs of the type involved in each case, the contractor must give a performance *and* payment bond. In each of these cases, however, the Court refused to read into the bond the statutory requirement that the bond given by the contractor contain payment provisions protecting the materialmen. According to the Court of Appeals for the Fourth Circuit, the statute could be read into the bond only if the statute expressly provided that its provisions were to be read into the bond. "But, in the absence of some such statutory provision, the Court will not read into a bond a [statutory] obligation which it [the bond] did not contain." *United States ex rel. Stallings v. Starr, supra* at 805.

This holding is no longer good law. Even Appellee concedes in argument III B that the provisions of a statute requiring a bond are, as a matter of public policy, read into bonds executed pursuant to the statute. Consequently, Appellee's federal cases, which stand for the proposition that statutory provisions cannot be read into statutory bonds unless the statute expressly provides that they shall be, are not valid statements of contemporary law. And, since the instant case is to be determined with reference to Arizona law, the Arizona Supreme Court's contrary decision in *Porter v. Eyer,* 80 Ariz. 169, 294 P.2d 661 (1956), is controlling.

As pointed out in Appellant's opening brief, the Arizona Supreme Court specifically held in *Porter* that statutory provisions in force at the time a statutory bond is executed are read into the bond as a matter of law. *Porter v. Eyer, supra* at 172, 294 P.2d at 663. Therefore, not only are the federal cases which Appellee relies on in support of its fourth argument no longer valid authority for the general proposition asserted, the conclusion they reach has also been specifically repudiated by the Arizona Supreme Court.

The Rhode Island case, *Glens Falls Indemnity Company v. American Awning & Tent Company,* 55 R.I. 284, 180 Atl. 367 (1935), is quite similar to the case presently before the Court

and its holding is directly contrary to the holding which Appellant asks this Court to make. However, Appellant contends that the *Glens Falls* decision is inconsistent with the Arizona decisions involving attempts of materialmen to reach a contractor's performance bond. There can be no doubt that the Arizona Supreme Court would, in light of its earlier decisions involving suretyship law, (see Appellant's Opening Brief pp. 16-21) reach a conclusion contrary to the Rhode Island holding.

The Rhode Island Court expressly refused to accept as controlling the same public policy considerations, also present in the instant case, which greatly influenced the Arizona Court's decision in *Webb.* Compare the Rhode Island Court's discussion of the policy considerations, 180 Atl. at 374, with the Arizona Court's discussion in *Webb v. Crane Company, supra* at 307-10, 80 P.2d at 703-04. The Rhode Island Court's requirement that there must be a provision containing a "specific undertaking to pay for labor and materials" which must "positively appear" within the bond or contract, 180 Atl. at 369, is a much more restrictive, stringent requirement than the Arizona Court's requirement that the bond or contract contain "a condition for their benefit." *Webb v. Crane Co., supra* at 310, 80 P.2d at 704.

Both parties to this appeal have agreed that it must be determined in accordance with Arizona law. Therefore, Appellee's antiquated cases from other jurisdictions which are contrary to Arizona law are totally irrelevant to the resolution of this appeal. Furthermore, the type of reasoning utilized in Appellee's cases was also rejected by the Arizona court in *Porter.* The Court held there that a mere performance bond could be and was converted into a payment bond because a statute requiring that a payment bond be executed had to be incorporated into the bond and it thereby became conditioned on payment as well as performance. Since the bond involved in the instant appeal specifically incorporated the contract, and since the contract required that a performance and payment bond be executed, *Porter* compels a

ruling that the Appellee's performance bond was, as a matter of law, also conditioned on payment. To paraphrase the Court's language in *Porter,* "we may presume that the intention of the parties was to execute such a bond as the . . . [contract] required." *Porter v Eyer, supra* at 173, 294 P.2d at 664. Appellee is, therefore, bound by the intent of the parties as reflected in the bond and contract and this intent is, as a matter of law, an intent to benefit third party materialmen such as Appellant. See discussion and cases in Appellant's Opening Brief, pp. 16-21.

ARGUMENT FOUR

APPELLANT IS ALSO ENTITLED TO RECOVER ON THE PERFORMANCE BOND BECAUSE THE BOND WAS INTENDED TO BENEFIT APPELLANT, AND EWALD, BY NOT FURNISHING A PERFORMANCE AND PAYMENT BOND AND BY NOT FURNISHING MATERIAL AS CONTEMPLATED BY THE CONTRACT, BREACHED TWO CONDITIONS OF THE CONTRACT, FULL PERFORMANCE OF WHICH WAS GUARANTEED BY THE BOND.

Appellee's fifth argument is to the effect that even though Ewald did not fully perform the contract, performance of which was guaranteed by the bond, Appellant cannot recover on the bond because it was not the obligee thereof. This argument completely overlooks the whole concept of third party beneficiary law by virtue of which a third party can acquire enforceable rights in a contract to which it was not a party or, more specifically, enforceable rights in a bond in which it was not the named obligee. Appellant demonstrated in its Opening Brief that under Arizona law a third party can recover on a contract or a bond to which it was not a party if it establishes that either document was intended to benefit it or a class of which it is a member, or if either document contains a condition for its benefit. Appellant also demonstrated that the bond and contract involved in the instant appeal did, as a matter of law, reveal an intent to

benefit Appellant so that it can recover thereon. Accordingly, since the contract incorporated into the bond contained several conditions for Appellant's benefit, these instruments were, in legal contemplation, intended to benefit Appellant. As Ewald, the principal on the bond, did not fully perform on the bonded contract, Appellant can recover on the bond as a third party beneficiary thereof.

CONCLUSION

Appellee has not, in most of its arguments, dealt with the facts presented by this appeal. Nor has it analyzed the cases upon which it relies or applied those cases to the facts actually presented. In its only argument which does deal with the fact that a performance and payment bond was contractually required, Appellee has relied on cases and reasoning which have been rejected by the Arizona Supreme Court even though Appellee has conceded that Arizona law must determine the outcome of this appeal.

Appellant has demonstrated that the bond and contract upon which this suit is grounded were, as a matter of law, intended to benefit Appellant. Appellant has also shown that the bond involved herein was, as a matter of Arizona law, conditioned on both performance and payment. In addition, Appellant established in pages 19-21 of its Opening Brief that Arizona public policy favors protecting materialmen who furnish supplies on public projects which cannot be liened by letting them recover on performance bonds if the bonds, like the instant one, contain a condition for the materialman's benefit. Appellee did not deal with this contention at all. Finally, Appellant has shown that the performance bond involved here was, as a matter of Arizona law, intended to benefit Appellant so that the principal's nonperformance of the contract renders the Appellee liable to Appellant on its surety bond.

Under any of these three theories, Appellant is, as a matter of law, entitled to recover on the bond. Therefore, Appellant

respectfully requests that this Court enter an order reversing the judgment entered by the District Court and directing that judgment be entered for Appellant on its Second Motion for Summary Judgment.

Respectfully submitted,
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I certify that, in connection with the preparation of this brief, I have examined Rules 18, 19, and 39 of the United States Court of Appeals for the Ninth Circuit, and that, in my opinion, the foregoing brief complies with those rules.

____
Earl E. Weeks

I certify that I delivered three copies of the foregoing brief this ______ day of __________________________, 1968 to:

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